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NOTES AND MEMORANDA.

THE NEW GERMAN BANK LAW.

The law of March 14, 1875, which transformed the old Bank of Prussia into the Reichsbank, was a remarkable piece of legislation. That it should have been based on the previous experience of Prussia, England, and other countries, is not strange, nor the fact that it contained some attempted improvements. The remarkable element was the foresight shown in the adaptation of the Reichsbank to the work which it had to do.

It was intended to create not only a central bank which should bring order and efficiency into the chaotic banking methods resulting from the multiplicity of State banking laws, give every needed stimulus to the anticipated industrial growth of the empire, and at the same time serve as an adequate regulator of the international movement of gold, but also a political instrument working towards the definitive consolidation of the German states into an imperial unity. It was to be a great bank, but at the same time an arm of the imperial government. In this respect the legislation is comparable with Alexander Hamilton's measures for the organization of the federal treasury, the assumption by the United States of the State debts, and the establishment of the United States Bank. If Hamilton's bank was not permanent, this was through no fault of his. While it lasted, it worked powerfully both towards political unity and the development of a sound and rational banking system. The success of the German plan has been even more marked, and its permanency seems assured. The influence of the Reichsbank in strengthening the imperial sentiment throughout Germany has been wholly satisfactory. The necessity of a centrally localized responsibility for the maintenance of the monetary standard, for the regulation of the gold movement within and without the country, and for the

elastic adaptation of the volume of currency to the industrial need for credit, has been convincingly shown. The force of opposition to the delegation of such large public powers to a private institution has been largely neutralized by the fact that the shareholders have only an advisory power in the conduct of the bank, and by the still more telling fact that, beyond a moderate dividend, the lion's share of the profits goes to the government.

The aim of the government in the original law was to secure a monopoly of note issue for the Reichsbank. This could not be done absolutely, owing chiefly to the strength of the particularist sentiment in the German states outside of Prussia. Various provisions in the law, however, placing restrictions upon other banks, forced many of these banks to give up their right of issue. In the mean time the spread of the use of deposits subject to check induced still other banks to renounce their issues, in order to secure freedom from the restrictions of the law. There remained seven of the original thirty-two banks of issue. The attempt to secure entire uniformity in the note circulation failed therefore of complete success. It succeeded so far, however, that, of the total amount of 385,000,000 marks of tax-free uncovered notes allowed for the empire, the contingent of the Reichsbank had increased, through the accretion of the contingents of the banks withdrawing from the system, from 250,000,000 to 293,400,000 marks before the passage of the new law.

The provision of the original law for regulating the amount of uncovered notes by laying a tax at the rate of 5 per cent. per annum upon them when in excess of a fixed limit must also be regarded as only a partial success. It has frequently happened that, when the market discount rate was 4 per cent. or even as low as 3 per cent., the Reichsbank has been forced to exceed its quota of uncovered notes, actually paying the tax of 5 per cent. on notes issued against loans on which it received only the lower rate. It was forced to do so by the fact that it could not afford to keep out of the market altogether. And it has done so when its metallic reserves were unusually large and there was no need for extraordinary precaution. The fact is that the men who devised

the system did not adequately forecast the enormous expansion of German industrial and commercial activity. The limit of uncovered notes, at first adequate, became entirely too small to enable the bank to hold its proper place in the system. On the other hand, in order to protect the gold supply of the empire, the bank has often had to raise its rate of discount above 5 per cent., when its uncovered issues were far below the limit. In other words, there has not been that influence of the tax upon the discount rate which, it was believed, would exist. The general lowering of the rate of interest has been another of the facts of recent economic development which the originators of the Reichsbank did not foresee.

Perhaps the most serious difficulty of the Reichsbank has been the practice of other banks of issue to cut its discount rate. This has enabled these banks at all times to keep out the greater part of their contingent of uncovered notes, being relieved from the necessity of guarding too carefully their own reserves by their ability at any time to draw upon the cash of the Reichsbank by rediscounts. Thus the burden of rendering safe the issues of the other banks falls in reality upon the Reichsbank. These issues remain in circulation as a practically fixed inelastic amount, which embarrasses greatly the efforts of the Reichsbank at critical times to defend its gold reserve, and tends to increase the fluctuations in the notes of the Reichsbank, already excessive. The uncovered notes of other banks are in effect not true bank-notes, but, like our national bank-notes, have no elasticity and act as a constant menace to the central gold depositary, which in Germany is the Reichsbank, and here is the federal treasury. The private or State banks of issue in Germany raid the reserves of the Reichsbank by bringing commercial paper there to be rediscounted. The national banks here raid the United States treasury by bringing in greenbacks and treasury notes for redemption.

The original law provided that every ten years, beginning with 1891, a renewal of the privilege must be had. This necessitated, under the requirements as to notice, the passage of the new law before the close of the year 1899. At these ten-year periods the imperial government has the right to wind up

the affairs of the Reichsbank or to purchase the stock at its par value, as well as to terminate the issue privileges of the other banks. Ten years ago the State Socialists agitated strongly for the exercise by the government of its option to purchase the stock. It was thought that the same proposal would again come to the front. But this party last year did not favor government purchase, because they thought such a pure State bank would simply strengthen the present Jingo policy of the government. And, as a matter of fact, the advocates of State ownership made no determined fight.

The government bill, arranged by agreement between the governments of the various states, after receiving the sanction of the Bundesrat, was introduced into the Reichstag the 21st of January, 1899. The Emperor in his speech from the throne very justly described it as a simple reform in certain unsatisfactory details, not as a radical change. The bill proposed an increase in the capital by 30,000,000 marks, making the total capital 150,000,000 marks; the raising of the surplus from 30,000,000 to 60,000,000 marks; the increase of the Reichsbank's quota of uncovered notes to 400,000,000 marks; the reduction of the ordinary stockholder's dividend to 5 per cent., before the division of profits with the imperial treasury (the law of 1889 had already reduced it from 8 to 6 per cent.); and the prohibition of a rate of discount by the private banks of issue lower than the rate of the Reichsbank. This last provision was suggested by the Bavarian government, although one of the strongest private banks is in Bavaria. The bill, after the first reading, was referred to a committee of twenty-eight members. Here a thorough discussion of its provisions was had. The opposition were not united. The Agrarians had no hostility to the last-named proposal, there being no private banks of issue in north-east Germany, where they are strongest. They were in favor of strengthening the power of the imperial government in the bank. They proposed government purchase of all the stock, the increase of the capital to 200,000,000 marks, government ownership of the new stock in any event, or the absolute limitation of private shareholders' profits. But none of their proposals was accepted. They were allied with the bimetallic interests; and their general aim

was to secure the larger circulation which they thought would result from a pure State bank, much as the "agrarian" party in this country thinks to secure cheap credit through government paper in place of bank-notes. The strongest opposition was that in behalf of the private banks of issue. South German chambers of commerce and other commercial interests were strenuous in opposing the prohibition to cut the Reichsbank's rate of discount. The committee finally compromised on this point, although the imperial government and the Reichsbank were urgently in favor of complete prohibition. The compromise was as follows: the Reichsbank must not cut its official rate when this is as high as 4 per cent.; and, when it discounts below its official rate, it must publish the fact in the *Reichsanzeiger*. The private banks, under penalty of losing their right of issue, must not discount below the Reichsbank's official rate, when that is as high as 4 per cent.; nor otherwise discount more than one-fourth of 1 per cent. below the official rate, nor more than one-eighth of 1 per cent. below the Reichsbank when it cuts its official rate.

The committee further changed the bill by fixing the amount of capital at 180,000,000 marks, and the limit of untaxed uncovered issue at 450,000,000 marks, and by reducing the shareholders' ordinary dividend to $3\frac{1}{2}$ per cent. Profits in excess of this, after the surplus reaches 60,000,000 marks, are to go one-fourth to shareholders, three-fourths to the imperial treasury. The new stock is to be divided into shares of 1,000 marks instead of 3,000, one-half of them to be sold by the end of 1900 and the remainder by the end of 1905. Any premium on the new stock will go into the surplus fund. The new stock is to be sold in open market, and not to the holders of the old stock, in order to forestall criticism that the bank is owned by a ring of capitalists. The Reichsbank, further, is to pay to the imperial treasury by January 1, 1901, an amount equal to the par value of the notes of the old Bank of Prussia still in circulation.

The bill passed the second and third reading on April 27 and 28, and was accepted by the shareholders of the Reichsbank at an extraordinary general meeting held at Berlin, May 28.

It is thought the provisions in regard to discount by the

other banks of issue will lead some of them to relinquish their right of issue, so that uniformity of bank-note circulation will be still more nearly approached. The preponderance of the Reichsbank in the system is greatly increased by the large addition to its contingent of tax-free uncovered notes, the entire increase from 385,000,000 to 541,600,000 marks for the empire going to the Reichsbank. The brilliant success of the Reichsbank in meeting the most trying difficulties has won for it almost unlimited public approval; and the changes of the new law are all in the nature of a vote of confidence, equipping it more adequately for the larger tasks it has now to perform with the vast growth of Germany's commercial and industrial interests. No radical change was found necessary.

One very striking fact is the absence of any important opposition to the Reichsbank on the part of the great deposit banks, which are naturally its rivals. This is to be explained in part by the rapid development of deposit banking in Germany, due to a really marvellous expansion of business, which has afforded ample room for profitable deposit banking. But, further than this, explanation must be sought in the special service which the Reichsbank performs for these other institutions. They need have relatively small concern for their own cash reserves so long as the Reichsbank stands as the centre of the system, ready at all times to rediscount their holdings of paper at need. The Reichsbank has become thus what the Bank of England is to the other English banks, or the Bank of France to its great banking clients,—a bank of banks.

The banking system of Germany presents certain striking analogies to that of the United States. In some degree, similar conditions, economic and political, have existed in both countries during the century. Germany was belated in her economic development as compared with England and France, and in many respects was not so advanced as the United States. In the main, the two countries were in nearly the same stage of progress. In Germany, political unity was scarcely an ideal until after Napoleon's conquest; and real union of sentiment was not yet achieved in America. In both countries, however, during the second third of this century, the new economic order was silently working towards a closer

union, industrial and political. During this same period the banking of the two countries was in a chaotic state, owing largely to the conflict of state laws. A multitude of private banks of issue was the result, with reckless rivalry in note issue. Uniformity in notes or in their regulation was alike foreign to the systems of the two countries. The Civil War wrought the basis for true political union of the United States, and a few years later the German states found themselves united as the outcome of a great war. The National Banking Law was a measure which aimed to strengthen the central government while unifying the system of note issue. Such was likewise the German law. Both systems were not really new creations, but the outgrowth of previous experience and development,—the adaptation of old principles to changed facts. In the main, the two systems are in line with the political opinion of the two countries. In Germany the one central institution is designed to dominate the banking business of the whole country. In the United States, free banking, under a general law, leaves the separate banks to work out their own union through voluntary association in clearing houses. In the United States, however, the ultimate gold reserve, which in Germany is in the Reichsbank, is kept by the federal treasury,—an anomalous condition, and not a satisfactory one. Aside from the degree of control over the banking system exercised by the federal government,—and it is by no means slight,—the central regulating power is found in the New York Clearing House. While not centralized in law, the banks have centralized their business to a remarkable degree,—a fact often overlooked by European critics. Centralization of business, as all experience shows, is a necessity of modern banking. The American system has demonstrated that this centralization is consistent with free banking; *i.e.*, may be wrought out by a kind of federative process, in which the dominance of a great central bank is not essential. Our system conforms to the republican idea of government, as the German system is in harmony with the idea of personal government.

The new legislation in Germany is a model of conservative change to meet the demands of progress. Our system needs

relatively few changes to make it conform to the present conditions. It needs a provision for elasticity in the note circulation, involving the abandonment of bond security. Uniformity it already has, and this would not be impaired if State banks submitting to the requirements of the federal law were allowed in the system. The necessary centralization could well be made secure and perfected by a legal recognition of the New York Clearing House as the guardian of the gold reserve, together with some degree of active participation by the Comptroller of the Currency in the work of the Clearing House. This latter change would tend better to keep the banks cognizant of their public duty, and to maintain the necessary connection between the government's finances and the business of the country. All of these changes would be the natural outgrowth of our experience. We want, not to tear down, but simply to make strong where we have found weakness, the system which we have, and which accords with our economic and political ideals. For procedure on this principle the German government have just afforded us an object-lesson in their new banking law.

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BRITISH TAXATION: IMPERIAL AND LOCAL.*

During the last few years there has been a lively discussion in Great Britain as to the relation between national and local taxation, in consequence, to a large extent, of the considerable changes effected by recent legislation. It is only within the last twelve years that the machinery of local government has received its present form. The act establishing county councils in England came in 1889, and was followed by the creation of county councils in Scotland a year later. Parish

* *Memoranda, chiefly relating to the Classification and Incidence of Imperial and Local Taxes.* (Royal Commission on Local Taxation.) London, Eyre & Spottiswoode, 1899. Folio, 250 pages. Price 2s. Parliamentary Blue Book, No. C.-9528.